



County of Los Angeles CHIEF EXECUTIVE OFFICE

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March 16, 2011

To: Don Knabe
Supervisor, Fourth District

From: William T Fujioka
Chief Executive Officer

A handwritten signature in black ink, appearing to read "W. T. Fujioka", is written over the printed name of the Chief Executive Officer.

COUNTY INVENTORY REDUCTION EFFORTS

As requested, ISD has reviewed the MTA report entitled "Update on Inventory Reduction Efforts." The MTA report identifies how they have used software, improved planning, and master agreements to reduce supplies inventories and costs. The County has implemented similar efficiencies to reduce costs.

During the 1990's, the Internal Services Department (ISD) restructured its materials management operations to eliminate major warehouses and implement just-in-time deliveries. Since then, ISD has continued to expand the use of master agreements and group purchasing to reduce costs and improve operations.

During the last several years, the County has implemented the eCAPS procurement and inventory modules. These applications position the County to more fully realize procurement volume efficiencies and pricing discounts that come with a single shared countywide database. As of July 1, 2011, only the Departments of Health Services (DHS) and Public Health will remain to be implemented. DHS is working closely with ISD, the Auditor-Controller, and this Office to implement eCAPS, along with the Global Healthcare Exchange (GHX) supply chain software, to reduce costs. The first DHS facility to implement eCAPS procurement and GHX, Olive View Medical Center, is scheduled to go live on July 1, 2011.

The attached report discusses these County purchasing initiatives in greater detail.

"To Enrich Lives Through Effective And Caring Service"

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Supervisor Don Knabe
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If you have any questions, please contact me, or your staff may contact Ellen Sandt, Deputy Chief Executive Officer, at (213) 974-1186 or esandt@ceo.lacounty.gov.

WTF:EFS:TT
JS:ef

Attachment

c: Executive Office, Board of Supervisors
 County Counsel
 Auditor-Controller
 Health Services
 Internal Services
 Public Health

Attachment
County Review of Metropolitan Transit Authority's report:
"Update on Inventory Reduction Efforts," dated March 3, 2011

Introduction

In the above referenced report, the Metropolitan Transit Authority identifies how it has used software, improved planning, and master agreements to reduce supplies inventories and costs. Since 1995, the County's approach has been to reduce inventory through eliminating and/or consolidating warehouses, and migrating to just-in-time (JIT) contracts.

The Internal Services Department (ISD), in coordination with the Chief Executive Officer (CEO, formerly CAO) and Auditor-Controller, implemented various actions in response to 1995 Board instructions, a 1997 State Auditor Report, 1997 Quality and Productivity Commission recommendations, and a 1998 CEO/A-C Administrative Policy on Inventory Practices. These actions have realized cost savings and revenue totaling \$20.4 million (one-time), and an estimated \$5.3 million annually thereafter, by eliminating or reducing County warehousing of inventory.

Several County departments continue to independently warehouse inventory, including the Department of Public Works, Sheriff, Fire, Probation, Health Services, and Public Health. These departments' inventory levels of on-hand supplies have been reduced by the establishment and use of JIT contracts.

The countywide implementation of the inventory and fixed asset components of the eCAPS procurement module will eliminate disparate inventory systems, improve the County's ability to control and track issuance of goods, and link the reordering of goods to the procurement module. The Fixed Asset module improves the link between fixed asset records and purchases, and improves the ability to monitor and track fixed assets.

County Policy Direction on Inventory Reduction

In October 1995, on motion of Supervisor Yaroslavsky, the Board of Supervisors ordered a review of County warehouse operations and authorized a consultant study of countywide warehousing with the goal of reducing warehouse and delivery costs. In a subsequent memo to department heads in January, 1996, Supervisor Yaroslavsky instructed departments to focus on achieving savings through:

- The elimination of unnecessary work (e.g., stocking shelves, performing inventories, intra-county deliveries, etc.) by acquiring supplies when they are needed directly from vendor;
- The reduction of waste due to obsolescence;
- Improved efficiency in necessary warehouse facilities; and
- The sale or better use of County-owned real estate.

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Deloitte and Touche completed the Countywide Warehousing Study in August, 1996. The study found that the County had far more warehouses than needed, the materials management system in the County was costly and inefficient, and that departments did not recognize the true costs of their warehouse operations. The Study's recommendations fell into two major categories:

- Expansion of commodity agreements, which include direct vendor delivery to the job site as an alternative to County warehouse and distribution of equipment and supplies; and
- Improvement of County materials management operations.

The findings and recommendations of the Deloitte and Touche report were supported by subsequent studies of County warehousing practices by the California State Auditor General, and by the Productivity and Quality Commission in November, 1997.

In response to the State Auditor's report, the Auditor-Controller and CEO jointly distributed a January 5, 1998, Administrative Policy on Inventory Practices. This required immediate implementation of the improved practices outlined in the policy, including the removal of excess and obsolete stock, and the implementation of just-in-time delivery practices to reduce or eliminate warehousing.

The following represent the actions taken to comply with the above directives:

Central Warehouse Closure

With 40 budgeted positions, the Central Warehouse stocked and distributed more than 2,650 different items with an annual value of \$38.4 million and delivered supplies to over 900 County locations. Materials handling fees of between 14.4 % and 16.4% recovered the Central Warehouse's annual operating budget. During Fiscal Year (FY) 1995-96, ISD Purchasing established and implemented JIT agreements for items stocked by the Central Warehouse, including fresh and frozen foods for the Sheriff and Probation departments, office, medical/surgical, janitorial and kitchen supplies, and printed forms. ISD closed the County's Central Warehouse in June 1996. The resulting savings to County departments were \$11 million for FY 1996-97 and \$4.5 million annually thereafter.

Surplus Warehouse Closure

Under State law, the Purchasing Agent (ISD) is responsible for the disposal of surplus County personal property. Historically, ISD operated a 27,000 square foot County Surplus Warehouse as a collection and disposal point for surplus property. In November, 1997, the Board of Supervisors approved the Purchasing Agent's recommendation to delegate to departments the responsibility to dispose of surplus County equipment directly from their facilities.

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As a result, ISD closed the County Surplus Warehouse in June, 1998 and eliminated three budgeted warehouse positions, which saved \$118,081 in salaries and benefits.

The closure of the Central Warehouse, the consolidation of ISD's Purchasing and Central Services operations at the Eastern Avenue headquarters, and the June, 1998 closure of the Surplus Warehouse resulted in the sale of the 19.7 acre Commerce facility complex at \$9.6 million.

Additional ISD Warehouse Closures and Conversions

Not including the Central Warehouse, ISD once operated eight internal warehouses totaling over 64,000 square feet with an inventory value of over \$4 million.

A detailed inventory of the remaining warehouses revealed the following:

Obsolete and Excess Stock

- 61% of the \$4,077,921 inventory value was obsolete or excess:

Obsolete Stock	\$ 939,625	23%
Excess Stock	1,561,367	38%
PC Maintenance Warehouse Stock*	<u>50,000</u>	1%
Total	\$2,550,992	62%

- Obsolete stock ranged from 15% to 21% of the total inventory value vs. 10% industry average per Deloitte and Touche.

Inventory Turnover and Low Cost/Low Issue Items

- Inventory turns (values of Inventory issued vs. value of on-hand inventory) were minimal.
 - ISD annual turns are less than 1 (.96 in FY 1995-96 and .82 in FY 1996-97 vs. Auditor-Controller/CEO standard of 6 to 12 turns. Liquidation of obsolete and excess stock would increase turns to only 2.34.
- Inventory issues (number of times items issued per year) were minimal.
 - Only 15% of ISD's inventory items were issued 13 or more times per year; 45% were issued only one or two times per year.
- ISD inventories contained approximately 1,200 low cost, low issue active items that had a total book value of \$52,361 (1% of the total inventory value). Low costs, low issued items are not cost effective to maintain as stock items.

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Following a review of its internal materials management operations, ISD initiated a project to liquidate warehouse stock, implement JIT vendor deliveries and convert specific warehouses to non-stock delivery sites (receipt-distribution points) at its major locations.

During FY 1997-98, four of the warehouses were closed, and inventory was reduced by more than half. Thereafter, agreements were established for building, telecommunications and computer operations supplies. In 1999, two of the four remaining receipt-distribution points were closed, and all ISD inventory, with the exception of low-dollar pantry stock, was eliminated.

Savings and revenue realized through this project are as follows:

	<u>One Time</u>	<u>Annual</u>
Central Warehouse closure/elimination of stock inventory	\$6.5 M	\$4.5 M
ISD Warehouse conversion/elimination of stock inventory	\$4.3 M	\$0.6 M
Surplus Warehouse closure		\$0.2 M
Sale of Central and Surplus Warehouses	<u>\$9.6 M</u>	
 Total savings/revenue	 \$20.4 M	 \$5.3 M

Throughout the years, ISD has continued to establish and refine processes for inventory reduction and elimination by expanding JIT agreements. In 2002, ISD implemented a Purchase Card (P-Card) program that provided craft services and building maintenance personnel the ability to purchase materials (e.g., building materials, electrical and industrial supplies, etc.) for County projects from retail outlets, such as the Home Depot. Based on a national agreement with the Home Depot established by the U.S. Communities-Government Purchasing Alliance, the County receives a 2% rebate on all P-Card purchases made from the Home Depot.

eCAPS Procurement Module

Background and Benefits from eProcurement

The implementation of a countywide automated procurement system is designed to:

- Standardize the County's purchasing processes in an electronic format and environment to provide County departments with consistent on-line access to procurement information and services.
- Streamline the procurement process through automation.
- Provide a tracking and reporting mechanism for the purchase of goods and services.
- Reduce purchasing lead times, increase productivity, and lower costs.

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In addition, the integration of financial and procurement data within eCAPS has the following benefits to County departments:

- A common chart of accounts, vendor/customer tables, and other data elements across departments for ease of reporting and ease of training users.
- A single set of systems equipment, software and databases for ease of maintenance and economies of scale in operation.
- Leveraging the use of a single business intelligence tool (Cognos) and a common reporting database structure across all financial and procurement applications.
- Consistent application of County purchasing policies and procedures through security, approvals and workflow.
- Enhanced capabilities to monitor purchases and activity from requisition to payment.
- Enhanced reporting and procurement analysis capabilities both within and across departments.

These features also permit better centralized oversight over County purchases and greater purchasing savings overall, including:

- The ability to preclude unauthorized purchases by County departments through systems security workflow and approval processes.
- The ability to establish, restrict and control items purchased by County departments through automated agreement catalogs of commodity groups (e.g., standardized products, formularies, etc.). A quantifiable example would include the formulary established and resultant results from the County's Office Supplies agreement with Office Depot in 2010. Based on the County's annual office supply expenditures of \$4.5 million, annual savings are estimated at \$425,000.
- The ability to analyze departmental purchase trends and spending habits on a countywide basis to identify additional areas where aggregating purchases to establish agreements via competitive solicitations will result in cost savings.

Current Systems Roll-out Status

To date, all but nine County departments have been trained and implemented on the eCAPS procurement module. Seven of the nine remaining County departments or organizations are scheduled to be implemented on July 1, 2011:

Beaches and Harbors
Child Support Services
Community and Senior Services
Parks and Recreation

Probation
Public Library
Public Social Services

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Due to their unique requirements, only the Departments of Health Services (DHS) and Public Health will remain after July, 2011. The CEO, Auditor-Controller, and ISD are working closely with DHS to implement e-Procurement at DHS facilities, with the Olive View Medical Center being the first DHS facility scheduled for implementation in July, 2011.

The completion of the eProcurement project will position ISD to more fully realize procurement volume efficiencies and pricing discounts that come with a single shared countywide database. Customer access to purchasing data also reduces calls and visits to the procurement office, thereby saving a significant amount of staff time. The management of the procurement process is enhanced by the ability to track requisitions/submissions throughout the process.

Department of Health Services – Purchasing Supply Formulary

The DHS e-Procurement implementation will also include the rollout of a purchasing supply formulary by the DHS Supply Chain Management Office. Key deliverables include the development of a standardized supply formulary, implementing controls to ensure compliance with the established formulary, reconciling and cleansing purchasing data for consistency and completeness and hosting established supplier agreements and pricing to automate the reconciliation of purchases to the supply formulary.

On September 21, 2010, the Board approved a sole source Agreement with Global Healthcare Exchange, L.L.C. (GHX) for the provision of supply chain procurement and data management services for DHS. GHX is a Business Exchange consisting of healthcare providers and healthcare product vendors. The primary members of GHX, including DHS, are also the members of the University HealthSystem Consortium (UHC). DHS has maintained membership in UHC, a not-for-profit member alliance of approximately 107 academic medical centers and its medical commodity contracting division, Novation, since approved by the Board in 1997. As a member of the UHC, DHS has the ability to access the UHC agreements as an alternative to the County conducting a competitive solicitation.

The purpose of GHX is to provide each member current procurement data regarding medical supplies, and assist members with maintaining a uniform and efficient supply formulary for medical and surgical supplies. As a member of UHC, DHS benefits from group discounts for all medical supplies covered under UHC established vendor contracts. DHS can increase its savings and utilize its buying power more effectively by using the GHX procurement data management services.

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The Agreement with GHX will enable DHS to manage a supply formulary and vendor contracts for DHS commodities, as well as create a tracking mechanism for the Department's purchasing history. In addition the Agreement will maximize supply chain automation, ensure compliance by implementing controls and standards, and provide the Department with the data necessary to effectively manage the supply chain process.